REPORT ON THE CHIGNECTO-CENTRAL AND STRAIT REGIONAL SCHOOL BOARDS BY THE MINISTER'S REVIEW COMMITTEE

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Report of the Minister's Review Committee

INTRODUCTION

During October 2001 it came to the attention of the Department of Education that officials of the Chignecto-Central Regional School Board (CCRSB) had authorized expenditures of approximately $1.7 million during the summer of 2001 without the knowledge of the elected board. The board conducted an investigation into the matter and the role played by those involved.

During the same period the Department also became aware that, in November 1998, the Strait Regional School Board (SRSB) had provided a $500,000 loan guarantee to the Royal Bank in support of the personal indebtedness of the Superintendent of the board. The board had commenced an investigation into the matter and the role played by those involved.

The Minister of Education responded to these events by requiring the boards to provide written reports outlining what had occurred and, in addition, the Minister appointed a review committee consisting of officials from the Departments of Finance, Justice and Education (the review committee). The report of the CCRSB is attached to this report and the SRSB report is outstanding at the time of writing as the board investigation is not complete.

ROLES AND RESPONSIBILITIES

Mandate and Role of the School Board:

The school board is accountable to the Minister of Education and is primarily responsible to investigate, act and report on the matters associated with the expenditure of funds.

The Education Act provides:

64 (1) "A school board is accountable to the Minister and responsible for the control and management of the public schools within its jurisdiction in accordance with this Act and the regulations."

64(2) "A school board shall, in accordance with this Act and the regulations,

> (ab) provide for the effective and efficient management of the financial affairs of the board;"

Mandate and Role of the Review Committee:

The review committee was created under the Minister's authority pursuant to the Education Act that states:

141(k) "The Minister is authorized to effect improvement generally in the conduct and administration of school boards, and, among other things, consult with, assist and advise school boards, develop proper methods of school board administration, financing, accounting and auditing, and collect, compile and disseminate education statistics and information."

The mandate of the review committee is to advise the Minister as follows:

- Comment on the internal control environment and identify the weaknesses therein which permitted these events to occur, and to provide recommendations for corrective actions thereof;
- To provide assurances to the Minister that following identification of these matters, that the boards have:
    - taken appropriate measures to fully investigate the events in question;
    - evaluated any options available to the board, either through civil or criminal actions, and recoveries thereof, and;
    - established appropriate control environments at the board level to prevent recurrence.

The review committee has reported based upon the information provided to the time of writing. It should be noted that it is possible, and perhaps probable, that corrective measures taken by the boards such as the ongoing forensic review and the replacement of key senior staff may identify other issues subsequent to the issuance of this report that were not known to the review committee during its review.

PROCESS FOLLOWED BY THE REVIEW COMMITTEE

The review committee has received the full co-operation of board staff and elected board members in conducting this review. Meetings were held with selected board members and senior staff during October – November 2001, as required.

Events Giving Rise to this Review:

Following is a summary of the events that have occurred in each of the boards. This is integral to understanding the control breakdowns that occurred permitting these events to happen, as well as subsequent discussion of recommendations.

Chignecto-Central Regional School Board:

- Discussions with the board indicated that during the summer of 2001 the board Superintendent, Mr Elmer MacDonald, directed the spending of $1.7 million without the express approval of the board as required by board policy. Rather than providing a control mechanism, the Chief Financial Officer (CFO), Mr Robert Renouf, participated in these events. Subsequent review by the board determined that the expenditures were made for valid educational purposes, however they were not made in accordance with board policy and on subsequent review the concern arose that the geographic distribution of the expenditures did not reflect equity in the distribution of education spending. The board was denied the discretion of determining how these funds would be expended.

- The funding to permit the redirection of expenditures described above was made possible from two practices. First, senior staff accrued purchase orders at March 31, 2001 to fully expend excess budget funds available in that year. No legal commitment existed for these purchase orders. Available funding arising from these practices was then utilized at the sole discretion of the Superintendent, without board oversight.

- The reporting of pensionable service to the Teacher's Pension Board with respect to the Superintendent included the Superintendent's travel allowance of approximately $24,000 per annum. Pensionable service is generally comprised of income or salary only, and clearly should not include elements of expense reimbursement. This resulted in a significant overstatement of the Superintendent's rights to retirement benefits under the plan on retirement.

- The Superintendent had instituted a practice of permitting the cashing of unused vacation days. Senior staff were permitted to receive payment for unused vacation in lieu of time off. The board was not aware of this practice although, in the case of the Superintendent, a clause to that effect existed in the employment contract signed by the board. The cashing of vacation days was particularly questionable in the case of retiring employees. Any justification that may exist for this practice is based on the inability of staff to access time off due to work commitments and is not relevant to retiring staff.

- The Superintendent negotiated a personal services contract with the CFO of the board setting out the employment rights and benefits of the CFO. The board had no awareness that the Superintendent had provided this contract either in advance or by way of information reporting after the fact. Identification of the contract only came to light as a result of other matters.

Strait Regional School Board:

- The board issued a guarantee to the Royal Bank of Canada in November 1998 in support of the personal indebtedness of the Superintendent, Mr John Sullivan, in the amount of $500,000.
    - The guarantee was signed by the board chair at the time, Mrs. Marie Campbell, the CFO - Mr John Cameron, and witnessed by Mr Bruce MacKeen, a local solicitor. It is a standard bank guarantee document. Key clauses stating the amount, and identifying the indebtedness as that of Mr John Sullivan, have been initialled by the signatories.
    - Issuance of the guarantee was made without the awareness of the board at large. The then Chair has indicated a lack of appreciation for the nature of the document signed.
    - Existence of the guarantee was not disclosed in the board's financial statements at the time or subsequently.
    - The Education Act does not authorize a school board to make a guarantee.
- Compensation arrangements surrounding the Superintendent and CFO were not subject to any meaningful review or oversight by the board. This is best illustrated by examples:
    - The Superintendent's employment contract contains a clause making the terms of the contract confidential to the officers of the board only and therefore not privy to the board at large, the Department of Education or the public. The existence of confidentiality clauses within personal services contracts are not consistent with principles of open disclosure and legislative requirements for disclosure.
    - The Superintendent's contract first negotiated in 1996 with a five-year term was renegotiated in 1998 after only three years. There did not appear to be any board motivated rationale for this renegotiation or appreciation of the fact that the original contract had not expired. The subsequent contract issued in 1998 contains a substantial escalation in the benefits extended to the

Superintendent.

- There did not appear to be any evaluation of the total compensation provided under the contract but rather a focus upon base compensation only. The sum of compensation provided to the Superintendent and CFO greatly exceed the market price for similar positions in the public sector when the value of payments made under travel, professional development and other clauses are factored in.

- Compensation contracts of both the Superintendent and CFO contain clauses that do not reflect the best interests of the board. The ability of the Superintendent to receive severance on completion of the contract term but without being terminated is an example. External professional support in the development of the contracts is not evident.

- Reporting of salary and benefit information reported to the Department of Education and the Auditor General misrepresents the actual payment of salary and expenses at the board.

- The board had entered into a number of commercial arrangements and partnerships that are not directly related to the provision of core public education. Board senior staff also served in executive positions in these organizations.

Discussion:

Internal controls are established for the broad purpose of protecting an organization's assets and exist within the framework of several key principles. A fundamental principle of any control system is that there is an adequate division of duties and powers between individuals such that no one individual has the power to access the organizations assets inappropriately, or that if this occurs it is detected and reported.

A second principle is the need for an over-riding governance structure where there exists an appropriate level of inquiry and review of the actions of staff in the performance of their duties. An element of trust is not inconsistent with this model provided that it co-exists in an environment of reporting and accountability.

The school board environment is one in which there is a high degree of concentration of power with a relatively small number of senior administrative staff. In this environment it is critical that the concentration of powers be offset by a strong accountability for the performance of staff by the board. In each of the instances under consideration by the review committee, there existed a high degree of trust in the senior management of the board prior to the events in question.

Responsibilities of organizations with respect to internal control and compensation review are commonly addressed through an audit or human resource committee that fulfills the board's obligations of inquiry and review in greater depth. Such committees should be fully informed of the manner and style of management compensation in place both at inception and as revised from time to time. Such a committee should not be dependent upon the information being brought for their review but rather must maintain an inquisitive and demanding mindset to ensure awareness and policy compliance. First and foremost it was the opinion of the review committee that the most significant issue that emerged was the need for improvements in the governance of school boards to insure that accountability is achieved. This is not to say that many boards do not have effective governance structures that respond to their obligations, including internal controls. It was not evident, however, that boards demanded accountability from management in all cases. A distinction is made between proactive management teams choosing to provide accountability information to boards and boards demanding accountability. This difference is critical to understanding how there can be well functioning boards in many cases or with respect to other responsibilities, yet have events of this magnitude occur.

It is a significant challenge for part-time board members to address the responsibilities inherent in the oversight of organizations with budgets as large as $250 million. Board members have varying degrees of experience and expertise with respect to governance in large organizations. In some cases, individuals may be reluctant to challenge a professional managerial team to be accountable, or may lack the expertise to evaluate complex contracts.

The review committee identified a strong need for a support network to enhance the accountability framework in boards. Improvements in this area could take many forms. For example, with respect to compensation issues in the provincial sector, the Public Service Commission fills the role of providing independent professional advice, maintaining consistency and relativity standards, as well as ensuring contractual terms are aligned with the best interests of government. Exercise of such a support role would have prevented the employment contracts that were extended in the case of the SRSB or the ability of the CCRSB Superintendent to extend an employment contract to the CFO without review or awareness of any other party.

RECOMMENDATIONS

- The review committee concurs that all personal services contracts entered into by school boards be subject to Department of Education approval prior to execution by the board. This recommendation provides reasonable assurance that contract terms, wage levels and responsibilities are subject to a consistency test across boards and that appropriate negotiations are reached in all cases.

- The review committee concurs with the need for a review by the public Service Commission of senior staff compensation across Nova Scotia school boards. Such review should include evaluation of the consistency and relativity of compensation across school boards, the appropriateness of the manner and style of compensation employed by school boards, review of the contractual terms evident in contracts to ensure that board rights have been adequately established and address the reporting and monitoring structures which exist to ensure that instances of conflict and self benefit are not permitted to occur.

- The review committee identified the need for there to be controls surrounding a board's ability to participate in commercial arrangements, either directly or indirectly, that fall outside of core public school education. Irrespective of the above, boards should not engage in activities that fall outside of the Education Act.

- School boards should be required in all cases to establish audit committees with clearly understood roles and responsibilities. Such committees should be tasked with oversight responsibilities, provide a more in depth forum for satisfying the board's internal control responsibilities, and enhance communications with the board, auditors and management with the objective of creating an environment where senior management is accountable for their actions on an ongoing basis.

- The Department of Education should expand the annual salary and expense report to include a direct representation from the audit committee that the report includes all compensation of employees.

- The Department of Education should evaluate its role in the oversight of school boards. Such an evaluation should reflect a view towards extending the departmental oversight of boards to include the effective administration and governance of boards.

- The Department of Education should require that a staff representative participate in the negotiation of board superintendent contracts. At present, the department has involvement in hiring and periodic performance evaluation but no role in the establishing and renewal of contracts.

- The Department of Education should evaluate the cost-benefit relationship in extending the external audit to include the board salary and expense reports filed annually with the Department of Education.

- The review committee supports the release of a revised school board financial handbook to provide increased consistency and accountability in board reporting and accounting.

- The review committee endorses the appointment of the forensic review of the SRSB. Such a review is required to fully investigate the events that have occurred, to identify recoveries and claims that can be exercised to minimize the losses of the board, to evidentially support potential recovery claims that may be initiated by the board, and to protect the board from further liability or claims from other parties.

- The review committee concurs that the Chief Financial Officer of the SRSB be a mutually agreeable selection of the board and department with a clear accountability relationship to the Department of Education, until such time as a satisfactory control environment is established.

INVESTIGATION AND RECOVERY ACTIONS OF THE BOARDS

The review committee was satisfied in the case of both boards that procedures had been put in place to adequately investigate the events that had come to light and also that the boards broadened their investigations when it became apparent that management had not acted in the board's best interests. Both boards utilized the services of external legal services to lead their investigations in the initial stages, with additional support being obtained by way of a review of the implications on their external audit at the CCRSB performed by Grant Thornton, and a forensic audit being conducted at the SRSB by Price Waterhouse Coopers. These reports are outstanding at this time.

CCRSB correspondence accompanying the report addresses the matter of whether the actions of officials were of a criminal nature and states that there are no grounds for pursuing a criminal investigation. As for the SRSB, we have noted that the board has requested a criminal investigation by the RCMP.

Both boards are giving full consideration to recovery options from the individuals in question for amounts where personal liability can be established, and have or will take legal counsel as to the merits of any potential civil action. Consideration of a possible insurance claim is also relevant in the case of SRSB.

Finalization of the external reviews above may also result in further actions by the boards for recovery.

As well as addressing the immediate need to investigate the matters that had arisen, both boards recognized the need to make longer-term improvements to evaluate and correct the weaknesses giving rise to these events.

CONCLUSION

The review committee has provided a number of recommendations for improvements in the accountability framework in school boards. In addition, the review committee notes the value in follow-up of the recommendations and findings that are anticipated from work being conducted by the Public Service Commission with respect to compensation and accountability, the Grant Thornton review of audit implications in the CCRSB and the Price Waterhouse Cooper's forensic review of the SRSB.

Collectively, these recommendations offer significant improvements in the control environment of boards.

MINISTER'S REVIEW COMMITTEE

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